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Hungary: A Progress Report

An Intelligence Assessment

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*Information as of 18 April 1979 has been used
in preparing this report.*

This memorandum was prepared by the Office of
Political Analysis in collaboration with the Office of
Economic Research. Any questions and comments
may be directed to

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**Hungary:
A Progress Report**

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Key Judgments

A year after deciding to take bold steps toward economic efficiency, the Hungarian leadership appears to be moving ahead without hesitation to reduce enterprise subsidies, to raise consumer prices and revamp wholesale prices, and to redistribute scarce labor supplies. [REDACTED]

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The mediocre economic results for 1978 have, if anything, reinforced the leadership's determination to confront economic problems head on. Since the first of the year, Hungarians have had some taste of the austerity that lies ahead, and although there have been no problems, a degree of risk clearly exists. The Soviets may have some qualms, but can hardly be displeased that the Hungarians are trying vigorously to cope with their economic problems. [REDACTED]

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Party leader Kadar remains the unquestioned master of the Hungarian political scene. Despite numerous rumors that the economic reform will cause personnel changes in the upper reaches of the leadership, there appears to be general support for the stringent measures. The regime has, however, made changes at lower levels of the bureaucracy and this is likely to continue as the search intensifies for better qualified people. [REDACTED]

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Hungary: A Progress Report

Rigorous Economic Policies

Beginning last April and continuing through 1978, the party Central Committee approved a number of severe measures designed to make Hungarian enterprises and workers perform more efficiently. The measures reflect the country's pressing need to:

- Conserve costly and increasingly scarce raw material imports, especially oil.
- Produce better quality goods to pay for imports of technology and raw materials from the West and to satisfy an increasingly finicky Soviet market.
- Use nominally scarce labor supplies more efficiently.

The regime's plans for dealing with these constraints include:

Cutting back drastically state subsidization of enterprises. This will be done through price and tax reforms and will make it more difficult for marginal enterprises to turn a profit, forcing them to become more efficient. Some taxation changes have already been made and the wholesale price structure is to be revamped by 1980. Domestic prices of energy and export-quality industrial goods will rise to the world market level.

Liquidating or merging enterprises unable to adjust to the more stringent conditions. Early this year, the government reportedly notified 30 enterprises they would be shut down and their personnel reassigned unless their operations became profitable within six to 12 months.

Dismissing excess workers or those who are disciplinary problems. Through this measure, the regime hopes to uncover pockets of underemployed labor and prod other workers into working better. The first of these reductions was made last February, reportedly on the personal decision of Kadar. The action allegedly shocked some party members and has undoubtedly caused some anxiety among workers, but there is no evidence that any disturbances took place. More reductions are planned.

Implementing, perhaps by 1981, an overall increase in consumer prices of upwards of 10 percent. A commission, under the leadership of ex-Politburo member Rezso Nyers, recommended in early 1978 that prices of politically sensitive basic foodstuffs increase by 20 percent. To remove some of the sting, wages would be increased by a small amount (400 forints—about a 12-percent increase in the average monthly wage for industrial workers). The first step in this program was apparently taken in January, when prices were raised on a small number of consumer goods.

Encouraging greater wage differentiation as an incentive to better work. The Central Committee last December bluntly called for an end to a "harmful egalitarian outlook."

Changing foreign trade mechanism, perhaps only organizational tinkering or a major expansion of the number of enterprises with foreign trade rights. There apparently are differences concerning the long-term expansion of trade with the West. The country's record foreign trade deficit last year helped prompt the removal of the foreign trade minister and may indicate that other policy changes are near at hand.

Poor Showing in 1978

Failure last year to meet key economic goals, especially to hold the line on domestic consumption has given further impetus to the regime's stringent economic policies. Domestic consumption increased 7 percent over 1977 instead of the planned 2 percent. The volume of investments rose by 4 percent, while the plan projected a decrease of 1.5 percent. Overall economic growth rate of 2.6 percent was among the lowest in East European countries.

Foreign trade problems compounded the difficulties as trade with the industrial West logged a record deficit. Exports to nonsocialist countries, valued in forints, increased less than 4 percent, while a 12- to 13-percent rise was predicted. Imports increased 15 percent while the plan called for only 3 to 5 percent. By the end of 1978, Hungary's hard currency debt to the West rose an

25X1 estimated \$1.8 billion from a year earlier, while the current account deficit rose from \$800 million in 1977 to \$1.4 billion in 1978. []

Austerity Ahead

Budapest has decided to correct the imbalances of 1978 by curbing the growth of income, investment, and imports this year. The economic plan for 1979 begins a period of austerity scheduled to extend into the 1981-85 plan period. The growth of national income is slated to drop from 4 percent in 1978 to less than 3 percent in 1979. Consumption is scheduled to grow very little, while the rate of investment should be half that of the previous year. The emphasis is on the development of quality exports to the West. Credit restrictions have been approved, profit taxes increased, and profit retention reduced in an attempt to lower domestic demand.

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The people are going to feel the sting of many of these measures. To help pave the way, party and government officials have been talking bluntly about the period of economic austerity that lies ahead. While the effort carries some risk, the Kadar regime probably is better suited than any in Eastern Europe to deal with it. []

25X1 Kadar has earned some personal popularity and considerable good will on which he can draw for public toleration. Given the decentralized nature of the economy, many changes will be implemented piecemeal, minimizing the chances of widespread unrest. The Hungarian leadership is also tactically astute and can be expected to go slowly when necessary. []

The Leadership

25X1 Kadar's command of the Hungarian party appears as firm as ever. The 66-year-old leader met with Brezhnev in Moscow in early March, unaccompanied by any advisers, to discuss economic cooperation in the 1980s and, [] Kadar's plans for widespread personnel changes in Hungary. The Soviet leader reportedly agreed to Kadar's proposals on cadre changes.

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Exactly what changes Kadar may have in mind is difficult to anticipate. He made some very important changes

of top-level people a year ago, and it would be uncharacteristic of him to follow these so closely with more changes at the top. []

25X1 Despite the opportunity for differences over the new economic policies, the leadership appears to be more united than in the past on the necessity for economic stringencies. Politburo member Sandor Gaspar, who has previously spoken out against price increases and in defense of the urban workers' interests, seems inclined to go along with current policy. Gaspar's trade unions, for instance, publicly supported the layoffs that began in February. Trade with the West could be a divisive issue, but an article published last May by the Politburo's conservative ideologue—Dezso Nemes—on the necessity of such trade suggests there may be general consensus in the Politburo on this matter. []

25X1 The apparent unity on overall economic policy, of course, does not exclude the possibility of differences over specific issues or opposition in the generally more conservative lower party ranks. [] there are differences over what kinds of concessions Hungary should be prepared to make (perhaps, such as the release of economic data) in the interests of expanding trade with the West. []

25X1 There may be a perceived need to bring new blood into the top leadership, but there is no obviously pressing reason to do so before the next party congress, which should convene next year. Speculation in this regard has and will focus on the Politburo's conservative old guard—Nemes and Antal Apro—and perhaps on such long-time Kadar cronies as Gaspar and Bela Biszku, who was displaced as number-two man last year. On the other hand, Kadar may be reluctant to make high-level changes, because these people are known quantities with whom he has worked well for many years and who represent different political currents. []

Lower Level Changes

25X1 The possibility of extensive changes at lower levels of the party and government seems much more likely. Speculation in this regard has derived in part from the appointment in April 1978 of two new key party secretaries (for economic affairs and for party cadres), both of whom have good reasons to press for personnel

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changes. The new man in charge of cadres, Karoly Nemeth, is also the new leading contender to succeed Kadar. He has an obvious need to create a personal following at lower party levels. The new party secretary for economic affairs, Ferenc Havasi, is a long-time foe of government bureaucrats, and he can now weed out those incompetents he battled in the past. [REDACTED]

There have been some personnel changes on these levels during the last year, but not extraordinary and mostly within the economic sphere. A number of subministerial changes were made late last summer. A recent Central Committee session approved two ministerial changes and gave promise of more shifts to come by criticizing unnamed "leaders" at all levels for inability to deal effectively with current economic tasks. The session also replaced the head of the party cadres department, tightening Nemeth's grip on the subordinate bureaucracy and perhaps providing a sign that changes in the party ranks may come soon. [REDACTED]

Extensive changes at the grass-roots level might have an impact within the leadership especially if there are people who want to stay Nemeth's hand. Changes could threaten the more "proletarian" and conservative elements of the party in favor of younger, better educated, and more pragmatic people. Those resisting at the lower levels could seek support from sponsors within the Politburo. [REDACTED]

The Soviets

On balance, Moscow is probably pleased that the Hungarians are making vigorous efforts to cope with economic problems. Although they are presumably uneasy about the risks involved, the Soviets must be thankful that Hungary (especially compared to Poland) is a bastion of political tranquility and relative financial prudence. There may be qualms about possible Hungarian plans to expand trade with the West, but since the policy is partially necessitated by Soviet economic constraints, the Soviets are not in a strong position to complain. Moscow is thankful that Kadar is a team player and probably is gratified that it is not being blamed for Hungary's economic slowdown. [REDACTED]

The main issue in Soviet-Hungarian relations at present appears to involve questions of economic cooperation in the early 1980s. Kadar's talks with Brezhnev in early March and a subsequent visit by Prime Minister Lazar in April appear to have focused on this subject. During these meetings, the Soviets reportedly agreed to increase oil deliveries to Hungary in 1981-85 by 5 to 10 percent annually in return for agricultural products (especially meat and corn) which Hungary could otherwise sell on Western markets. The Hungarians also obtained Soviet approval of a small trade credit covering purchases of other Soviet raw materials, especially timber and iron ore. [REDACTED] the Hungarians have agreed to provide greater assistance (including machinery and manpower) to develop Soviet raw materials in return for increased Soviet deliveries to Hungary. The increase of raw materials, however, could still be less than Hungary had requested. [REDACTED]

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